

C & K PETROLEUM, INC.
TWIN ARROW, INC.

IBLA 82-1331

Decided February 3, 1983

Appeal from decision of the Colorado State Office, Bureau of Land Management, declaring oil and gas lease C 8151-A to have expired.

Set aside and remanded.

1. Hearings -- Notice: Generally -- Oil and Gas Leases: Termination --
Oil and Gas Leases: Well Capable of Production -- Rules of Practice:
Hearings

No lease for lands on which there is a well capable of producing oil and gas in paying quantities shall expire because the lessee fails to produce, unless the lessee fails to place the well in a producing status within 60 days of receipt of notice to do so. Upon a BLM determination that a lease has expired at the end of its extended term because the well on the leasehold is not capable of production in paying quantities, the lessees of record are entitled to notice and an opportunity to request a hearing on the issue of the productive capacity of the well where they have presented evidence raising an issue of fact regarding the status of the well.

APPEARANCES: James D. Voorhees, Esq., and Ruth Brammer Johnson, Esq., Denver, Colorado, and Joe T. Hood, Dallas, Texas, for appellants.

OPINION BY ADMINISTRATIVE JUDGE IRWIN

C & K Petroleum, Inc., and Twin Arrow, Inc., have appealed the decision of the Colorado State Office, Bureau of Land Management (BLM), dated August 11, 1982, declaring noncompetitive oil and gas lease C 8151-A to have expired under its own terms on December 31, 1980. The BLM decision recited

that BLM had information from the Minerals Management Service (MMS) that well No. 4-14X in the NE 1/4 SE 1/4 sec. 14, T. 3 S., R. 101 W., sixth principal meridian, "is not considered to be producing in paying quantities."

Review of the case file reveals a memorandum dated July 29, 1982, from MMS to BLM reporting that well No. 4-14X is not considered to be producing in paying quantities and that lease C 8151-A expired by its own terms on December 31, 1980. There is no evidence or other information in the file providing any background for MMS' report.

In their statement of reasons, appellants assert the following with respect to well No. 4-14X:

The 4-14X Well was completed as an open hole well, which is a recognized means of completion in the area (Exhibit A). On March 12, 1979, a production test was performed testing the open hole interval in the well between 2,558 feet and 3,900 feet. The well produced .8 mcf of gas during the one-hour production test, resulting in a calculated production capability of 19.5 mcf per day. A well completion report evidencing the open hole completion and the production test was filed with the United States Geological Survey (Exhibit B). The 4-14X Well was, as of December 31, 1980, and is now, capable of producing gas in paying quantities.

(Statement of Reasons at 2). Appellants report that all gas produced from the well is dedicated to Northwest Pipeline Corporation (Northwest) at the highest applicable price permitted by the Natural Gas Policy Act of 1978, but that no gas has been sold because appellants lack a pipeline connection. Appellants' attempts at obtaining a pipeline have included:

1) An October 1979 application to construct a pipeline filed with BLM by Twin Arrow, Inc., the well operator, that was approved that October but rescinded in March 1980.

2) Efforts to get Northwest to install a pipeline and a report by Northwest that its application to build a line to another nearby well was rejected by BLM.

3) Another application (C-010-TU-82-32) filed by Twin Arrow, Inc., for a permit to install a line that is pending with BLM.

Appellants argue that, although the status of well No. 4-14X is shut-in, gas wells may be considered capable of producing and that its well is capable of producing in paying quantities. Appellants contend that 43 CFR 3107.3-2 requires that a lessee with a well capable of producing in paying quantities be given 60 days to put the well on producing status prior to a determination that the lease has expired and report that they have never been given such notice. Finally, appellants urge that they are at least entitled to a hearing on the issue of the productive capability of the well.

[1] Under section 17(f) of the Mineral Leasing Act, as amended, 30 U.S.C. § 226(f) (1976), an oil and gas lease in its extended term terminates by operation of law when paying production ceases on the lease, subject to three statutory exceptions. Michael P. Grace, 50 IBLA 150 (1980); John S. Pehar, 41 IBLA 191 (1979). The exceptions provide that no lease shall terminate for cessation of production if: (1) Reworking or drilling operations are begun within 60 days after cessation and are continued with reasonable diligence until production resumes; (2) the Secretary of the Interior has ordered or consented to suspension of operations or production; or (3) (applicable to this case) for lands on which there is a well capable of production, the lessee places the well in production within 60 days after receipt of notice to do so. See 43 CFR 3107.3-1, 3103.3-8, 3107.3-2.

As noted, BLM, upon recommendation from MMS, found simply that the well No. 4-14X "is not considered to be producing in paying quantities" and held the lease to have expired. Appellants have submitted evidence that the well is capable of producing in paying quantities but shut-in pending development of a pipeline to its purchaser.

Upon a determination that production has ceased on an oil and gas lease in its extended term by reason of production or drilling, because the well on the lease is no longer capable of production in paying quantities, the lessee of record is entitled to notice and an opportunity to request a hearing on the issue of the productive capacity of the well where it has presented evidence raising an issue of fact regarding the status of the well. Universal Resources Corp., 31 IBLA 61 (1977). In this instance it is appropriate to remand the case to BLM for referral to MMS. If MMS determines after review of appellants' evidence that there is no well capable of production in paying quantities on the lease, due notice shall be given to appellants by BLM advising them of the basis of the determination and that they may request a hearing before an Administrative Law Judge on the issue of the existence of a well capable of producing in paying quantities. If a hearing is requested, the case shall be transmitted to the Hearings Division, Office of Hearings and Appeals.

At any eventual hearing the burden of going forward with the evidence and the ultimate burden of proof falls on the appellants. They must establish the existence of a well capable of production in paying quantities. In John G. Swanson, 66 IBLA 200 (1982), we stated that

[i]n order for a well to be considered capable of production in paying quantities it must be physically capable of such production at the particular time in question, i.e., "where there has been production or where production can clearly be obtained but it is not because there is a 'lack of pipelines, roads, or markets for the oil and gas.'" American Resources Management Corp., 40 IBLA 195, 201 (1979). Actual production is not necessary in order for a well to be considered capable of production in paying quantities. On the other hand, the mere presence of a well will not suffice. Id. Not only must a well be physically

capable of production, Arlyne Lansdale, 16 IBLA 42 (1974), it must also be capable of producing "in paying quantities," i.e., sufficient quantities to yield a reasonable profit to the lessee over and above the cost of operating the well and of marketing the product. Amoco Production Co., 41 IBLA 348, 351 (1979); The Polumbus Corp., 22 IBLA 270 (1975); Kerr-McGee Oil Industries, 73 I.D. 110 (1966).

66 IBLA at 202.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision of the Colorado State Office is set aside and the case remanded for further action consistent with this decision.

Will A. Irwin
Administrative Judge

We concur:

Douglas E. Henriques
Administrative Judge

C. Randall Grant, Jr.
Administrative Judge

